

INTERVIEW PLAN
MAY 18, 1994

SUBJECT NAME:
COMPANY:
POSITION:
RESPONSIBILITIES:

**STATEMENT REGARDING NON-IDENTIFICATION OF COMMENTS AND
CONFIDENTIALITY:**

STATEMENT REGARDING PROVISION OF FINAL REPORT:

OBJECTIVE: To generate ideas, concepts and recommendations for strategies, mechanisms and vehicles to provide capital to minorities in telecommunications industries.

INTERVIEW TYPE: **PATTERN**

HYPOTHESES:

1. Telecommunications is an attractive sector for minority businesses.
2. Existing capital and capital sources are inadequate to meet the demand from minority businesses for start-up, expansion mature stage capital.
3. New and different approaches to supply capital to minority businesses are required.

TOPICS TO COVER:

1. Interest and involvement in minority capital formation and/or business development.
2. Interest and involvement in telecom.
3. Views on future of telecom.
4. Views on future for minorities in telecom.
5. Views on minority capital demand.
6. Views on capital supply for minority companies.
7. Ideas to improve capital supply for minority companies.

LEAD STATEMENT: As you know, I am working on a project to determine how capital availability may be enhanced for minority businesses in the telecommunications industries. I appreciate your spending the next half-hour with me to offer ideas and suggestions you may have which may assist minority companies access debt and equity capital in the future.

TOPIC 1. - Interest and involvement in minority capital formation and/or business development.

LEAD QUESTION: Lets begin by describing your interests and involvement in minority capital formation and/or business development.

FOLLOW-ONS: How long; what sectors; what activity; investment level.

TOPIC 2. - Interest and involvement in telecom.

LEAD QUESTION: Lets go on to describe your interests and involvement in telecom.

FOLLOW-ONS: How long; what sectors; what activity.

TOPIC 3. - Views on future of telecom.

LEAD QUESTION: Lets talk about the future - how do you see the telecom. industry evolving, developing and changing with respect to business opportunities.

FOLLOW-ONS: Market demand; products and services; regulation; competition; key success factors.

TOPIC 4. - Views on future for minorities in telecom.

LEAD QUESTION: How do your views on the industry at large differ, compare or change when looking at opportunities for minority businessmen in telecom.

FOLLOW-ONS: Market demand; products and services; regulation; competition; key success factors

TOPIC 5. - Views on minority capital demand.

LEAD QUESTION: Lets move to the capital side of our discussion.

How do you see the demand for capital on the part of minorities in telecom.

FOLLOW-ONS: In the future; sectors of high demand; start-up; expansion; mature.

TOPIC 6. - Views on capital supply for minority companies.

LEAD QUESTION: How does the demand for capital compare with capital sources for minority telecom. companies presently.

FOLLOW-ONS: In the future; sources of particular note; start-up; expansion; mature; problems.

TOPIC 7. - Ideas to improve supply for minority companies.

LEAD QUESTION: To summarize, there appears to be a gap between capital demand and supply. Let's conclude with your ideas on how to fix this problem.

FOLLOW-ONS: Immediate; near term; long term; start-up; community based; expansion; telecom specific.

BRIDGE: What other aspects of this problem should we be concerned with that we have not covered or discussed.

FOLLOW-ONS: What is your opinion of the questions we have asked; our process.

CLOSE: Thank you for your time and thoughts. You've been most helpful to our project. I hope you will not mind if I call to clarify or follow up on any points we've discussed today. We'd appreciate your comments on the final report document which you will receive upon its completion in the Summer. Thank you again.

EXHIBIT B

State of Texas

DISPARITY STUDY

A Report to the Texas Legislature as
Mandated by H.B. 2626, 73rd Legislature

December 1994

Prepared by
NATIONAL ECONOMIC RESEARCH ASSOCIATES, INC.

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We, of course, bear sole responsibility for the opinions expressed and conclusions reached in this report.

EXECUTIVE SUMMARY

The State of Texas Disparity Study was mandated by H.B. 2626 of the 73rd Legislature with overwhelming bipartisan support in both Houses. Using a methodology that is guided by decisions of the U. S. Supreme Court and other courts, the study assesses the experience of minority and woman-owned businesses in Texas and the effectiveness of the State's current program in assisting them. This summary introduces the study and describes its findings and its recommendations.

I. Introduction to the State of Texas Disparity Study

The State of Texas Disparity Study examines whether race and sex discrimination limits the ability of companies owned by minorities and women to do business with the State of Texas. It evaluates the

State's current measures for helping companies owned by minorities and women obtain business from the State. It also reviews possible measures for reducing the effects of discrimination, where found, on the ability of companies owned by minorities and women to obtain business from the State. Some of these measures have been used elsewhere but do not have proven records of success or failure. All of these measures have advantages and disadvantages which policymakers need to consider carefully.

The methodology adopted by the study was designed to be consistent with U.S. Supreme Court and other court decisions concerning the affirmative-action programs adopted by non-federal governmental entities. In 1989 the Supreme Court ruled, in *City of Richmond v. J. A. Croson & Co.*, that the City of Richmond, Va.'s minority business program, which set aside 30 percent of all construction dollars for minority businesses, was unconstitutional. The plurality decision, authored by Justice Sandra Day O'Connor, described the circumstances under which state and local governments could have race-based preferences. The government must be able to show that there is a compelling governmental interest in having race-based preferences and that the race-based preferences are narrowly tailored to remedy racial discrimination. The Supreme Court in the *Croson* decision, and several Courts of Appeal in post-*Croson* decisions, have emphasized that discrimination can be established through a combination of statistical and anecdotal evidence.

Definitions Used By The Study

For purposes of this study, the term *minorities* includes African Americans, Hispanics, Asians (including Asian Pacific, Asian Indian, and Asian Islanders), and Native Americans. The term *Historically Underutilized Businesses* (HUBs) refers to businesses that are at least 51 percent owned by minorities and/or women and in which the minority and/or female owners actively participate in the control and management of the business.

When summarizing the results, the study uses the four major categories of goods and services procured by the State: construction, commodities, professional services, and other services. Each of these categories consists of several industries. The study considered industries defined by the U.S. Bureau of

the Census at the two-digit SIC Code level of detail. Construction consists predominantly of building construction, heavy construction and special trade construction. Commodities consists of manufacturing, wholesale trade, and retail trade. Professional services consists of architectural, engineering, accounting, land surveying services as well as services provided by a licensed physician or optometrist. Other services includes insurance and real estate, research, management and consulting services, business services such as advertising, transportation services, repair services, legal services, personal services such as cleaners, social services, and educational services.

The State's Current HUB Program

In 1991, the State instituted the Historically Underutilized Business (HUB) Program to increase the opportunities available to companies owned by minorities and women to do business with the State. The study found that the HUB Program has had only a modest effect on the share of State procurement dollars received by minority and woman-owned businesses. The benefits of the program have not been distributed evenly, however. Depending on the industry, most of the increase in the HUB share went to Asians and white women. In general, the HUB Program has not increased the share of State business awarded to African American-owned businesses, and, in several industries, African-American businesses are receiving a lower share than before the Program started.

The study found evidence of discrimination against HUBs in Texas. This discrimination makes it harder for HUBs to compete for business from the State as prime contractors or subcontractors. The study found that African-American and Hispanic businesses are the most disadvantaged in seeking State business; businesses owned by white women are the least disadvantaged; and Asian and Native American-owned businesses fall in between.

What Are The Next Steps?

As required by H.B. 2626, this study is being distributed to all members of the Texas Legislature and all State agencies for their review and consideration. This study does not compel or require any particular course of action. It does raise important issues of public policy that State decision makers will

want to consider carefully. The manner in which the State responds to the findings of this study will be decided, of course, by members of the Texas Legislature and State agency officials.

The Texas General Services Commission is specifically authorized by H.B. 2626 to adopt appropriate rules to implement the findings and results of this study. Other agencies, whose procurements are outside the jurisdiction of the General Services Commission, do not have that specific authorization, but may desire to review their procurement processes to assess the need for modification. In addition, the Texas Legislature may determine that certain statutory changes are necessary.

As just mentioned, there is no single course of action that is mandated or required as a result of this study. The most prudent course of action for the State is one that considers a range of alternatives for remedying the effects of discrimination documented in this study. Alternatives, some of which have been used in other jurisdictions, include easing state bidding criteria that have a disparate impact on all small businesses, including those owned by minorities and women, creating programs that provide effective financial and technical assistance to small businesses seeking State contracts, enacting legislation that specifically prohibits discrimination in business transactions, and increasing the effectiveness of the existing HUB program.

Who Conducted the Study?

The State of Texas Disparity Study was conducted by National Economic Research Associates, Inc. (NERA) in association with Lannen & Oliver, Perkins Coie, Rincon & Associates and Ronquillo & DeWolf, LLP. NERA is an international economic consulting firm whose clients include many of the world's largest governments, corporations and law firms.

Professor Ray Marshall of the University of Texas at Austin and Professor George LaNoue of the University of Maryland at Baltimore County served as outside advisers to the study team. Professor Marshall has conducted disparity studies for the City of Atlanta and other state and local agencies. Professor LaNoue has served as a consultant to business groups that have challenged the constitutionality

of race/sex-based affirmative-action programs and the validity of disparity studies conducted in other jurisdictions.

The State of Texas Disparity Study was conducted entirely independently from a study by the Joint Select Committee on Historically Underutilized Businesses, a committee of State Senators and Representatives charged with monitoring the progress of State agencies in increasing their procurement from HUBs and with developing recommendations for policy change to assist HUBs. Their recently published report is entitled *The Texas Challenge: Broadening the Competitive Edge*.

What Evidence Did The Study Examine?

The Legislature appropriated \$1 million to conduct the study, and it took about a year to complete. The study reviewed approximately \$15 billion worth of State procurement during Fiscal Years (FY) 1989-1993 to determine the extent to which HUBs obtained business from the State directly as prime contractors or indirectly as subcontractors. This review was based on a detailed computer analysis of more than a million records of State expenditures. The study conducted statistical analyses of these data for the State as a whole, and also examined data at the agency level for seven large State agencies and institutions of higher education: the General Services Commission, Texas Department of Criminal Justice, the Comptroller of Public Accounts, Texas Parks and Wildlife Department, Texas Department of Transportation, the University of Texas (Campuses and System), and Texas A&M University (Campuses and System). We closely examined the procurement practices of all of these agencies and of four additional ones: the Texas Department of Human Services, Texas Department of Public Safety, Texas Natural Resource Conservation Commission, and Texas Department of Mental Health and Mental Retardation.

In addition to these and other statistical analyses, the study conducted in-depth interviews with 327 business owners, of all races and sexes, across the State. It examined more than 5,000 responses to a mail survey of businesses owners of all races and sexes across the State, and reviewed the relevant literature and case law as well as related studies.

What Does the Executive Summary Do?

This summary provides an overview of NERA's findings and methodology. After this introductory section, the next section summarizes the evidence collected by the study. The third section summarizes the different courses of action identified in the report that are available to the State to respond to discrimination where it is found. The final section gives general conclusions.

As this summary provides only an overview, the reader is strongly encouraged to read NERA's full final report ("The State of Texas Disparity Study"), which contains technical details on the data and methodology used for the study. The full report also presents many qualifications that affect the interpretation of the results and their implications for assisting HUBs.

II. What Did the Study Find?

HUBs have not fared as well as we would expect. That conclusion is based on consistent findings across race and sex groups and across industries from different statistical analyses of the relative success of HUBs:

- HUBs received a smaller share of State procurements between FY89 and FY93 than would be expected given their availability to do business with the State.
- Minorities and women earned less from their businesses in 1990 than would be expected given their qualifications. Moreover, minorities are less likely to own or operate a business than non-minorities with similar qualifications in 1990.

Generally, each of these statistical analyses showed that businesses owned by African Americans and Hispanics fared the worst, that businesses owned by white women fared the best (although still worse than white men), and, in most cases, that businesses owned by Asians and Native Americans fell between these two extremes.

Based on consistent survey findings across race, sex and industry groups from survey and anecdotal evidence, there is anecdotal evidence of discrimination that makes it harder for businesses owned by minorities and women to prosper:

- Almost 30 percent of minority business owners and almost 14 percent of white female business owners claim that they experienced at least one instance of discrimination in a business dealing in the last five years.
- A comparison of the responses of HUBs and non-HUBs to questions concerning the difficulty they have with various bid requirements shows that HUBs report more difficulty than non-HUBs. This is true even after controlling for differences in firm size and firm age between HUBs and non-HUBs.
- Many HUB owners report specific examples in which they have experienced discrimination.

Generally, the surveys and interviews find that African-American business owners report the highest incidence of discriminatory treatment and problems with bid requirements, white female business owners report the least, and Hispanic, Asian and Native American business owners fall somewhere in between.

How Well Have HUBs Done in Texas?

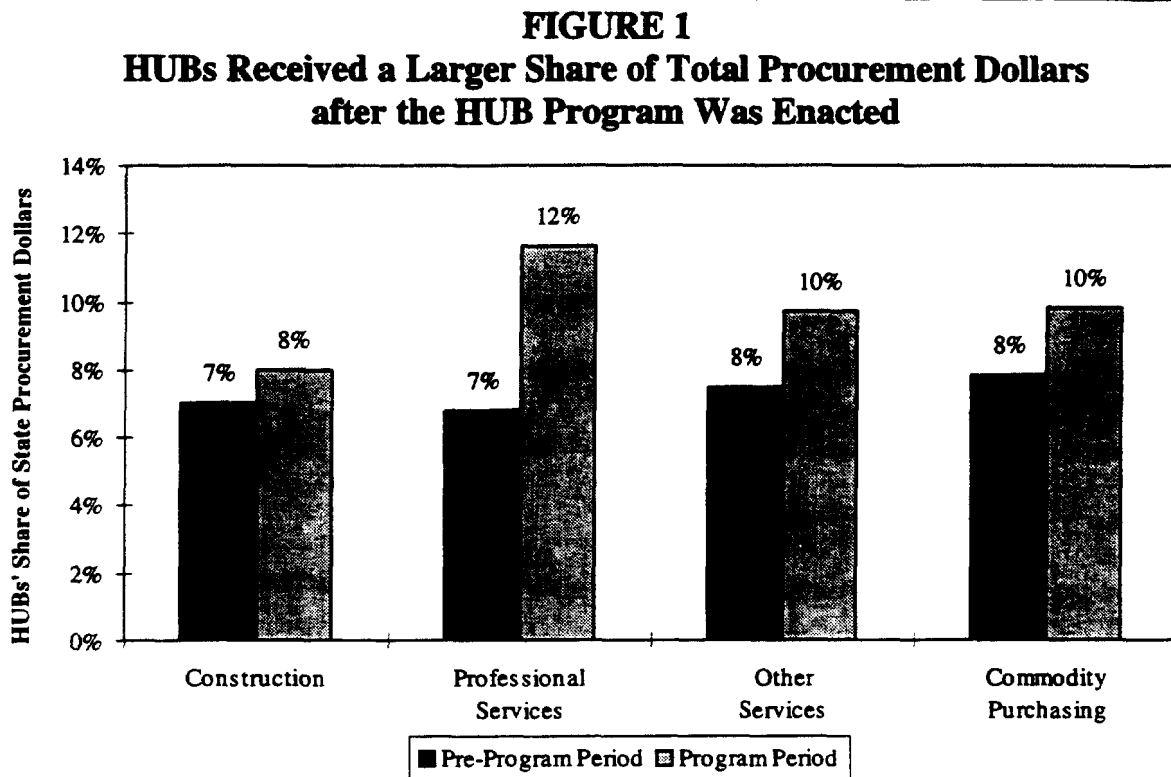
The study examined the *utilization* of HUBs by the State. It then determined the *availability* of HUBs in the State. Finally, it determined whether there was a *disparity* between HUB utilization and availability.

Utilization in State Procurements

The study analyzed payments by the State to vendors between FY89 and FY93. The State procures the bulk of its goods and services from firms in Texas—94 percent of construction dollars are received by Texas vendors, 75 percent of professional services, 66 percent of other services and 67 percent of commodities. Consequently, the study focused on procurements with Texas vendors.

Almost 190,000 Texas vendors were paid \$14.5 billion between FY89 and FY93. To determine which of these were HUBs, the study matched vendor names with a directory of approximately 26,000 HUBs constructed from more than 50 sources throughout Texas. Several surveys were conducted to verify and adjust the data to ensure that HUB vendors were accurately identified. Based on this analysis, the study found that HUBs received between 6.8 and 7.8 percent of the dollars in each of the major procurement categories before the enactment of the State's HUB program in 1991 (the pre-program period) and between

8.0 and 11.6 percent after the enactment of the program (the program period). These results are shown in Figure 1.



Notably, this apparent success of the program has not been felt by all minority groups. Specifically, while other groups have experienced improvements in their share of State contracting, African-American and Hispanic businesses have seen no improvement in most industries, and in commodities and professional services they are obtaining *lower* shares of State business.

The study was not able to obtain as detailed information on subcontracting. However, five State agencies—the Texas Department of Criminal Justice, the General Services Commission, University of Texas System, Texas A&M System and the Texas Department of Mental Health and Mental Retardation—maintained lists of subcontractors (but did not track dollars received by these subcontractors). Combining data from these agencies with the results of a survey of prime contractors, the study found that HUBs received 8.1 percent of the subcontracts in the pre-program period and 10.1 percent in the program period.

Availability of HUBs

The study calculated the percent of establishments—the unique physical location where business is conducted—owned by HUBs in the markets from which the State procures goods and services. It counted an establishment if it had at least one paid employee besides the owner. Each establishment of a multi-establishment firm is counted once in the pool of available businesses. The study found that, during the pre-program period, HUBs comprised 15.5 percent of the available establishments in construction, 19.7 percent in professional services, 30.4 percent in other services, and 12.3 percent in commodity purchasing. (The percentages were slightly higher in the program period.)

The study's definition of availability could be criticized for counting *too few* HUBs or for counting *too many* HUBs. Some could argue that it understates the availability of HUBs because many HUBs do not have paid employees but could expand if less discrimination generated more work. Moreover, they may argue that HUB availability is understated because it does not count the many HUBs that would form if discrimination were reduced. While this view deserves consideration for some purposes, its expansive definition of availability is not appropriate for determining whether there is current underutilization.

Others could argue that this definition overstates HUB availability because it counts too many small HUBs that do not have the qualifications to perform work for the State. This view ignores the fact, however, that discrimination against business owners make it difficult for HUBs to obtain these qualifications in the first place. Restricting the definition of availability to businesses with similar qualifications assumes that the problem of discrimination does not exist.

The study has taken a middle course between these two opposing views. Moreover, the study also undertook several additional analyses to determine whether lack of qualifications can explain the disparities described below. These additional analyses, described in the full report, found that:

- HUBs were underutilized even after controlling for certain qualifications of the businesses and their owners. HUBs are underutilized in most narrowly defined industries (so the study's findings are not a statistical artifact of examining broad procurement categories). For example, HUBs were underutilized to varying degrees in heavy

construction, building construction and specialty construction as well as in construction overall.

- HUBs are underutilized for small procurements (so the study's findings are not the result of assuming that HUBs are as qualified as non-HUBs to compete for large procurements).
- HUBs are also underutilized when the study focused solely on small businesses in the private sector (so again the study's findings are not the result of comparing small HUBs to large corporations).

Some have suggested using directories of minority and woman-owned businesses, lists of bidders with government agencies, and other business directories to calculate availability. There are problems, however, with relying on such lists. These lists are difficult and expensive to compile, they are invariably incomplete and the accuracy of other data in the lists is generally poor.

Unlike these data, the Census data relied upon by the study are based on IRS tax returns and Social Security tax reports to the Social Security Administration. These data are reliable because failure to file these forms or filing inaccurate forms can lead to criminal penalties.

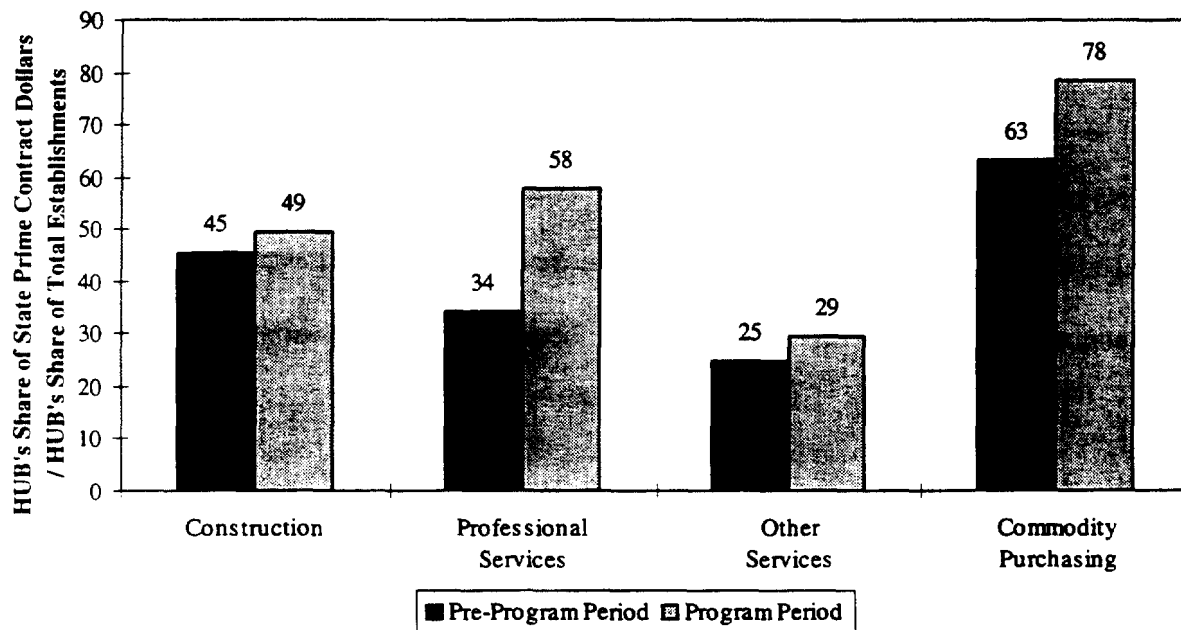
Finally, others have suggested availability measures that might be desirable in theory but that either cannot be implemented with existing data or that are based on samples that are not statistically reliable. For example, comparing availability and utilization at the level of four-digit SIC code industries (a narrow classification used by the Census) was suggested. Unfortunately, reliable Census or other data on HUBs are not available at this level of detail and too few contracts are awarded to each four-digit SIC code industry to constitute a statistically reliable sample for determining HUB utilization. For example, even at the two-digit SIC code level (a broader classification also used by the Census) considered by a portion of the study, there were many two-digit SIC code industries in which there were too few observations to allow one to draw statistically reliable conclusions. Therefore, it would be neither practical nor proper statistical practice to conduct the analysis at the four-digit SIC code level.

Disparities

The study compared HUB utilization and availability by calculating a *disparity ratio* for each race or sex group in each procurement category. A disparity ratio is simply the ratio of utilization to availability (times 100). A disparity ratio of less than 100 indicates that HUBs are used less than would be expected given their availability in the relevant market.

The study found that the disparity ratios for prime contracting were generally well under 100: HUB utilization was less than two-thirds of availability in every procurement category in the pre-program period and less than 80 percent in the program period. A summary of the disparities is shown in Figure 2.

FIGURE 2
HUB Disparity Ratios Are Less Substantial after the HUB
Program Was Enacted, but Disparities Remain
 (A ratio of less than 100 indicates a disparity)



The disparity ratios for subcontracting were also much less than 100: 42 percent in the pre-program period and 56 percent in the program period. The HUB program reduced, but did not eliminate, the disparities. In these subcontracting results, although there is uneven variation across groups, all groups did obtain an increased share of subcontracts with the enactment of the program. The disparity ratios for